Testimony of Chris Atkins, Director of Tax and Fiscal Policy at the American Legislative Exchange Council, Before the Congressional Democratic Budget Forum

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Good afternoon. My name is Chris Atkins and I am Director of the Tax and Fiscal Policy Task Force at the American Legislative Exchange Council in Washington, DC. ALEC is the nations' largest, bipartisan individual membership organization of state legislators. With more than 2400 legislative members nationwide, more than 1/3 of all state legislators are ALEC members. ALEC's mission is to advance the Jeffersonian principles of free markets, limited government, federalism and individual liberty among America's state legislators.

Thank you for inviting me to speak on the role the federal government has to play in the state budget crisis. I want to assume, for the purposes of our discussion, that it is appropriate for the federal government to take an active role in partnering with the states to help erase their budget deficits. I should note that ALEC in principle disagrees that Congress should take an active role in state deficit reduction. We have state sovereignty and federalism concerns with such an approach, not to mention the fact that it ignores the role the states themselves played in causing their own fiscal imbalance. For the purposes of our discussion, however, let's assume that the federal government has a constitutional and pragmatic role to play in easing state budget deficits.

The question then becomes what kind of assistance should Congress provide? Congress could provide a short-term fix that will potentially allow the states to get through another year, like the federal assistance package approved by Congress earlier this year. Congress could also take a long-term view and seek to change specific federal policies that impermissibly burden the states with federal mandates without also providing for federal financing. Or Congress could adopt a mix of short and long-term solutions. These are the options we face if we assume that Congress has a role to play.

I am sure that many of you have worked in state government, and understand the challenges that state lawmakers face in crafting and approving state budgets each year. State lawmakers, like those in the federal government, face voters who seem to hold conflicting demands: the people don't like to pay taxes, but they also like to have quality schools, health-care services for the poor and senior citizens, good roads, and public safety. Unlike the federal government, however, all states but Vermont are restricted from deficit-spending. States, therefore, do not have the luxury of passing tax cuts while simultaneously adopting farm subsidies, a new prescription drug plan, and prosecuting a war in Iraq. In the states, both sides of the ledger have to equal out.

I state these facts to you because it should inform the federal assistance package that you promote in Congress. Since states have recurring needs like schools, roads and health care for the poor, it is important that they have access to stable, recurring revenue streams to pay for those programs. The need to fund schools is not going to go away next year, so it is important that the revenues needed to fund schools not go away either.

This is the major problem with the short-term bailout you gave to the states in May. The $20 billion package was certainly welcome in most state capitals—though I should note that many ALEC legislators (Republicans and Democrats) were opposed to the package. The chief problem is that the states do not know what, if anything, they can expect next year from Congress. State lawmakers are unsure whether they will get another $20 billion, more or less than $20 billion, or anything at all. As you can see, there is a great amount of uncertainty involved in this type of federal assistance. Furthermore, a federal cash payments to the states becomes just another in a long and growing list of one-time fixes the states are employing, like accounting gimmicks, raiding tobacco settlement funds, and bond issues, which rose over 100% from 2002 to 2003.

And, of course, this all assumes that the states will use the money properly. Those who advocated for federal assistance earlier this year insisted that the money would replace federal obligations placed on the states, such as homeland security, No Child Left Behind, and Medicaid. Not all states used the money responsibly, however, despite the fact that the statute prohibited the states from using the money to enact new programs. Iowa, for example, used part of the federal money to enact a new "economic development" package consisting mostly of corporate welfare. Maine used part of the federal money to enact a new state prescription drug program. Louisiana was apparently so strapped for cash that they could afford to apply some of the federal money to a music festival in New Orleans. Many states that otherwise used the money lawfully still complained that the receipt of the federal money caused major disruptions in the state budget process by providing a new pot of cash to fight over.

That's not to say that the short-term solution doesn't have its benefits. It is immediate and allows states to forego planned spending cuts and tax increases. Its best feature is that it gives the states a quick reprieve until their own revenues get back on track. I should note that I am starting to become skeptical that states are going to recover all that quickly from their revenue shortfalls—at least not to the point where they were in the late 1990s. Most of the evidence points to a huge run-up in capital gains revenues in the states during the boom stock-market in the late 1990s—conditions not likely to be repeated anytime soon. So maybe we should stop betting on the economy to bail the states out of their fiscal crisis—at least not to the highs they reached in the late 1990s.

Let's compare the short-term solution with a more long-term fix that focuses on alleviating specific federal mandates placed on state governments. This approach compares favorably for the states, will provide more fiscal relief and ultimately be better for state budgets than another cash payment. But before we get into the comparison, I need to be specific about what kind of mandates I am talking about.

One of the best resources for the recurring federal mandates placed on state and local governments is a report on the subject issued in January, 1996, by the Advisory Commission on Intergovernmental Relations (ACIR). ACIR made a number of recommendations that would significantly ease the fiscal pressure placed on the states by federal law. However, the Unfunded Mandates Reform Act of 1995 does not reach or excludes from protection many of the mandates that ACIR recommended for elimination. Specifically, there are a number of well-intentioned federal laws that regulate state and local governments as if they were members of the private sector. Congress has already acted on a number of ACIR's recommendations, but if Congress wants to seriously help the states fiscal condition in a long-term fashion, the Unfunded Mandates Reform Act of 1995 needs to be re-visited with an eye toward strengthening the protections it contains for the states.

For example, Congress needs to consider raising the total dollar threshold when a state and local construction project becomes subject to the requirements of the Davis-Bacon Act. Congress should also consider waiving the Davis-Bacon requirements in cases where the federal dollar share of the project is small. Why should a state have to pay prevailing wage requirements on a project that uses federal funds for only 5% of total project costs? Isn't it more important that localities are able to quickly, efficiently and cheaply build more school facilities, rather than ensure that construction workers are paid the prevailing wage in the locality? I have spoken with a number of state lawmakers whose communities feel more threatened by this federal requirement, when it comes to education policy, than any other policy. It's time to remove a major federal impediment to the development of state and local public infrastructure, or at least raise the threshold requirements for triggering prevailing wage laws.

IDEA also continues to be a major fiscal headache for state and local lawmakers, and while not properly called an unfunded federal mandate, it is certainly an underfunded federal mandate. The federal government has failed to live up to its promise, made when IDEA became law and re-affirmed in 1997, to fund 40 percent of IDEA costs borne by the states. It is time for Congress to either live up to its promise, or allow the states greater flexibility in providing for the special needs of students. On this last point, please do not think that state lawmakers are unconcerned about education. It has been my experience that state leaders in both parties view education as an issue of fundamental importance, and have the expertise and the will to provide for the varying education needs of our students.

There are a number of other areas where Congress could relax fiscal pressure on the states, such as rethinking whether or when the Fair Labor Standards Act should apply to state and local governments and rethinking federal policy to force states to adopt certain laws by accepting federal highway money. A focus on relieving these and other specific unfunded mandates has none of the trappings of the short-term cash fix. One of the major problems with a cash payment is the fact that it is one-time. Relieving unfunded mandates, however, will provide fiscal relief to the states in perpetuity. It is a fiscal solution that state lawmakers can immediately apply to schools, roads and health care with a reasonable assurance that the assistance will continue. Raising the threshold for prevailing wage laws, for instance, will potentially lower the cost of public school construction in every locality in America. More schools mean more teachers and lower classroom sizes, a win-win for students and the public.

To conclude my remarks, I want to point out that ALEC has long called on Congress to relieve unfunded federal mandates. We may not agree with all the approaches discussed today, but we can definitely agree that Congress needs to do everything in its power to alleviate the fiscal burdens that it places on our states and local communities. As we continue to discuss this issue, I hope that we can continue to make progress in this area even in those times where states are relatively secure financially.

Thank you for listening and thank you for inviting me to speak today.